

Perspectives for Future Inter-Regional Trade Cooperation

Conference Sponsored by the Konrad Adenauer Stiftung

Washington, D.C.

25 November 2003

The failure at Cancun and the prospect for a complete collapse of the Doha Round of multilateral trade negotiations leads the trade ministers of the world to two mutually exclusive future paths – one path that is almost surely unproductive and the other path that is potentially quite productive. Unfortunately, the natural inclination of trade ministers is to choose the unproductive path because it avoids the hard choices and keeps them busy.

The unproductive path is to give up on the prospect for a successful multilateral round and to pursue a variety of regional and bilateral agreements in the name of free trade. But such agreements among countries that are not already major trading partners, by their nature, *distort* world trade, because they risk substituting the most efficient producer in the region for the most efficient producer in the world. The basic arithmetic of this problem has been understood since Jacob Viner's article on this issue over 50 years ago but without much effect. There may be *political* reasons for bilateral U.S. trade agreements with Israel, Jordan, Morocco, etc. but no apparent economic reason. I favored NAFTA, because Canada and Mexico were our first and third largest trading partners at the time of the agreement; in this case, the benefits of eliminating tariffs on the large volume of existing trade were much larger than the relatively small amount of trade that was shifted from outside of the region. The proposed Free Trade Agreement among the Americas, I suggest, makes no similar economic sense. For the United States, almost all of

our trade, other than with our NAFTA neighbors, is on an east-west basis with Europe and East Asia. The largest U.S. imports from Latin American countries south of Mexico are oil and cocaine, neither of which would be affected by a regional trade agreement. Such a regional agreement among countries that are not already major trading partners greatly increases the prospect that trade diversion from other regions would be larger than trade creation within the region. I will continue to oppose regional and bilateral trade agreements unless a strong case can be made that they serve an important political purpose.

The potentially productive path is to face up to the hard choice necessary for a successful multilateral agreement or to acknowledge the benefits of a unilateral reduction of trade barriers. Cancun failed because the governments of the developed nations were not willing to offer anything of value to the governments of the poor nations; specifically, they were not willing to make a commitment to reduce their absurd trade protections and subsidies on agricultural products. My judgement is that the necessary condition for saving the Doha Round is a joint prior commitment by Japan, the United States, and the European Union for a substantial phased reduction of these agricultural protections and subsidies; that is probably the only condition that would induce the governments of the poor countries to return to a multilateral negotiation.

In the absence of such a commitment, I suggest, the optimal trade policy for the United States, I suggest, is to make the case to the American people and to Congress about the value to the United States of *unilateral* reductions of current U.S. trade barriers. Someone other than trade ministers would probably have to make this case, because trade ministers have too long described a reduction of U.S. trade barriers as a *concession* to gain a corresponding reduction of the trade barriers of other countries, rather than an act that benefits the United States whether or not it induces a corresponding reduction of the trade barriers in other countries. The place to

start, I suggest, is to make the case to eliminate two of the most absurd U.S.- specific trade barriers: the 25 percent tariff on light trucks and the quota on imported sugar. The high tariff on light trucks was the U.S. response to the “chicken war” with Europe in the early 1960s, a tariff that was originally levied on VW pickups and vans as a retaliation for the high European tariff on chickens and is now levied only on those light trucks by the few Asian manufacturers who do not produce them in the United States. The quota on sugar leads the domestic wholesale price of sugar to be about twice the world price, has created the wholly artificial market for high-fructose corn syrup, and has led several American candy companies to move to Canada so that they can buy sugar at the world price. The elimination of these two U.S. trade barriers would not be without controversy, but such unilateral actions would do more than anything else to restore some credibility to the Bush administration’s free trade rhetoric.

In summary; my preferences for the *way* that trade barriers are reduced are in the following order:

1. multilateral trade agreements
2. unilateral reductions
3. regional trade agreements,
4. bilateral trade agreements.

For the moment, my primary concern is that a failure to achieve a successful multilateral agreement will lead to a proliferation of bilateral trade agreements.